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**SOAH DOCKET NO. 473-21-0538
PUC DOCKET NO. 51415**

APPLICATION OF SOUTHWESTERN	§	BEFORE THE STATE OFFICE
ELECTRIC POWER COMPANY FOR	§	OF
AUTHORITY TO CHANGE RATES	§	ADMINISTRATIVE HEARINGS

**CITIES ADVOCATING REASONABLE DEREGULATION'S
REPLY TO EXCEPTIONS TO THE PROPOSAL FOR DECISION**

**Alfred R. Herrera
Sergio E. Herrera
HERRERA LAW & ASSOCIATES, PLLC
4524 Burnet Road
Austin, Texas 78756**

October 28, 2021

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**CITIES ADVOCATING REASONABLE DEREGULATION’S
REPLY TO EXCEPTIONS TO THE PROPOSAL FOR DECISION**

The Cities Advocating Reasonable Deregulation¹ (“CARD”) hereby submit their *Reply to Exceptions to the Proposal for Decision* and in support thereof, show as follows:

I. Introduction/Summary [Preliminary Order (PO) Issues 1, 2, and 3]

CARD’s Reply to Exceptions is limited to exceptions the Southwestern Electric Power Company (“SWEPCO” or the “Company”) raised related to Section II of the outline presented in the Proposal for Decision (“PFD”) addressing Invested Capital – Rate Base.

With regard to other parts of SWEPCO’s exceptions, CARD respectfully refers the Administrative Law Judges (“ALJs”) to CARD’s prior briefings in this proceeding including its post-hearing initial and reply briefs, and CARD’s Exceptions to the PFD, and in particular Section III of the PFD’s Outline related to Rate of Return.

With regard to rate of return, SWEPCO raises no new issues not already addressed in CARD’s prior pleadings or soundly rejected by the ALJs. CARD continues to urge adoption SWEPCO’s proposed revenue requirement set forth in summary fashion in CARD Exhibit No. 6, the direct testimony of Mr. Karl Nalepa, including the cost of capital proposed by Dr. J. Randall Woolridge’s direct testimony presented in CARD Exhibit No. 4 and Dr. Woolridge’s recommended ROE OF 9.00%.²

¹ The Cities Advocating Reasonable Deregulation is comprised of the Cities of Atlanta, Bloomberg, Carthage, Center, Daingerfield, Fruitvale, Gilmer, Gladewater, Hawkins, Henderson, Hooks, Jefferson, Kilgore, Lakeport, Longview, Marshall, Maud, Mineola, Mt. Enterprise, Mt. Pleasant, Mt. Vernon, Naples, New London, Omaha, Overton, Pittsburg, Queen City, Red Lick, Texarkana, Wake Village, Waskom, Wellington, White Oak, Winnsboro and Winona.

² CARD will retain the outline set forth in the parties’ briefs for sake of convenience but its exceptions are limited to the discussion in the PFD regarding return on equity.

II. Invested Capital - Rate Base [PO Issues 4, 5, 10, 11, 12, 13, 14, 15, 16, 18, 19, 20, 21, 22]

A. Generation, Transmission, and Distribution Capital Investment [PO Issues 4, 5, 10, 11, 13, 14, 15, 16]

1. Dolet Hills Power Station [PO Issues 67, 68, 69, 70, 71]

CARD urges the Commission to approve the ALJs' recommendation to adhere to the Commission's recent precedent in Docket No. 46449³, and allow SWEPCO to earn a return of and on Dolet Hills between March 18, 2021 and December 31, 2021, but not thereafter.

The Commission's precedent from Docket No. 46449 prohibits a utility from earning both a return *on* and *of its* invested capital that is no longer *used and useful in providing service*.⁴ In this proceeding, Docket No. 51415, SWEPCO seeks the very relief the Commission denied it related to SWEPCO's generation plant, the Welsh Unit 2. In Docket No. 46449 the Commission denied SWEPCO a return *on* Welsh Unit 2 because its early retirement rendered the power plant unit no longer used and useful. In this proceeding, after December 31, 2021, SWEPCO's generating plant, the Dolet Hills power plant, like Welsh Unit 2, will not be used and useful in providing service to customers.

The record evidence makes clear that SWEPCO will retire Dolet Hills no later than December 31, 2021, thus rendering the plant no longer used and useful in providing service to ratepayers after that date. SWEPCO asserts that the Commission's Cost of Service rule requires that the Commission include Dolet Hills in its rate base because the plant is an element of SWEPCO's Test-Year data in this case.⁵ However, as the ALJ's correctly concluded at proposed Conclusion of Law No. 26, the Commission has discretion for good cause to make exceptions to its substantive rules applicable to electric-service providers, *including its Cost of Service Rule*,⁶ and here ample good cause exists: There is no dispute that SWEPCO is going to retire Dolet Hills within a few weeks after the Commission establishes rates in this proceeding; the record evidence

³ *Application of Southwestern Electric Power Company for Authority to Change Rates*, Docket No. 46449, Order on Rehearing at Finding of Fact Nos. 66 – 71 (March 19, 2019).

⁴ *See Id.*

⁵ *Application of Southwestern Electric Power Company for Authority to Change Rates*, Docket No. 51415, SWEPCO's Exceptions at 10 (Oct. 7, 2021).

⁶ *Application of Southwestern Electric Power Company for Authority to Change Rates*, Docket No. 51415, Proposal For Decision ("PFD") at Conclusion of Law ("COL") 26; *see also* 16 TAC § 25.3(b).

provides the data needed to determine the effect of removing Dolet Hills from rate base and provides the date by when SWEPCO will retire Dolet Hills thus undoubtedly comprising a known and measurable change to SWEPCO's invested capital.⁷

CARD reiterates the ALJ's observation regarding the timing of both SWEPCO's decision to retire Dolet Hills and its decision regarding when to file this rate case. Like the ALJs, CARD takes SWEPCO witness Mr. Brice at his word "in professing that SWEPCO did not time its filing to achieve any such tactical benefit, but was driven merely out of concern with the utility's perceived inability to earn a reasonable return in excess of its operating costs." However, the ALJs correctly point out that there can be exceptions to the Commission's Cost of Service rule when reason so dictates. Here, to conclude otherwise, would invite manipulation by utilities anticipating retirements of generation units.⁸

CARD urges the Commission to affirm the ALJs' reasoning. Allowing SWEPCO to keep Dolet Hills in rate base past December 31, 2021 and earn a return *on* and *of that plant* would burden ratepayers with the cost of a plant that will no longer be used and useful in providing service to ratepayers, a burden on top of the aftermath costs of Winter Storm Uri that ratepayers are having to bear. SWEPCO's proposal would require ratepayers to pay a return on \$122.8 million on a total company basis, or approximately \$45.4 million for its Texas Retail jurisdiction, for a plant that very well may no longer be used and useful in provider service before this Commission issues a final order in this proceeding.

Therefore, CARD urges the Commission to approve the ALJs' recommendation to follow the Commission's precedent in Docket No. 46449⁹, and allow SWEPCO to earn a return of and on Dolet Hills between March 18, 2021 and December 31, 2021, but not thereafter.

2. Retired Gas-Fired Generating Units [PO Issue 13]

CARD urges the Commission to approve the ALJs' recommendation to adjust SWEPCO's requested rate base to remove the net book values of its five retired gas plants¹⁰ and place those

⁷ 16 TAC § 25.231(c)(2)(F)(iii).

⁸ PFD at 51.

⁹ Docket No. 46449, Order on Rehearing at Finding of Fact Nos. 66 – 71.

¹⁰ The five gas-fired plants are Knox Lee Units 2, 3, and 4; Lone Star Unit 1, and Lieberman Unit 2. See PFD at 17-18.

values in a regulatory asset.

Similar to the treatment of Dolet Hills, SWEPCO's treatment of the undepreciated value of the Knox, Lone Star, and Lieberman retired gas plants is controlled by the Commission's precedent in SWEPCO's prior rate case, Docket No. 46449. Consequently, following the Commission's recent precedent, CARD urges the Commission to preclude SWEPCO from recovering through rates a return *on* the undepreciated value of the Knox, Lone Star, and Lieberman plants when they are no longer used and useful in service. Moreover, as the ALJs astutely point out in the PFD, SWEPCO offered no persuasive reason why Docket No. 51415 is different from Docket No. 46449.¹¹

Crucially, in the PFD the ALJs correctly point out that they themselves and the Commission must remain guided by the import of the Commission's holding and reasoning in its order in Docket No. 46449, that:

“[T]he interest of ratepayers and shareholders with respect to a plant that no longer provides service” are properly balanced by “[a]llowing [the utility] a return [of], but not [on], its remaining investment in that plant.”¹² Moreover, and perhaps more critically, the Commission reasons that a retired plant is not considered a “used and useful” investment that would be included in rate base under PURA and Commission rules.¹³

SWEPCO failed to present any evidence to show that its Knox, Lone Star, and Lieberman retired gas plants will be used and useful past their retirement date. Therefore, CARD urges the Commission to approve the ALJs' recommendation to follow the Commission's precedent in Docket No. 46449 and to adjust SWEPCO's requested rate base to remove the net book values of the Knox Lee Units 2, 3, and 4; Lone Star Unit 1, and Lieberman Unit 2 and place those values in a regulatory asset.

¹¹ See PFD at 25.

¹² Finding of Fact 69 in the Order on Rehearing in Docket No. 46449 states: “Allowing SWEPCO a return of, but not on, its remaining investments in Welsh Unit 2 balances the interests of ratepayers and shareholders with respect to a plant that no longer provides service.” Here, on page 24 of the PFD, the ALJs misquote the Commission's findings from Docket No. 46449, and reverse the placement of “on” and “of” and mistakenly state: “[a]llowing [the utility] a return *on*, but not *of*, its remaining investment in that plant.” Given that the ALJs have stated that the precedent established in Docket No. 46449 is binding in this case, CARD presumes the ALJs intended their quote to be consistent with the Commission's Order on Rehearing at Finding of Fact No. 69 in Docket No. 46449.

¹³ PFD at 24; *see also* Docket No. 46449, Order on Rehearing at Finding of Fact Nos. 66 – 71.

3. Coal and Lignite Fuel Inventories
 - B. Prepaid Pension & OPEB Assets [PO Issue 41]
 - C. Accumulated Deferred Federal Income Tax [PO Issues 20]
 1. Net Operating Loss ADFIT
 2. Excess ADFIT
 - D. Accumulated Depreciation [PO Issue 12]
 - E. Regulatory Assets and Liabilities [PO Issues 19, 21, 22, 41, 50]
 1. Self-Insurance Reserve [PO Issue 19 and 40]
 2. Hurricane Laura Costs [36, 37, 38, 39]
- III. Rate of Return [PO Issues 4, 5, 8, 9]
- A. Overall Rate of Return, Return on Equity, Cost of Debt [PO Issue 8]
 1. Return on Equity
 - a. Overview
 - b. Return on Equity

With regard to rate of return, SWEPCO raises no new issues in its exceptions not already addressed in CARD's prior pleadings or soundly rejected by the ALJs. CARD urges the Commission to adopt CARD's witness, Dr. J. Randall Woolridge's recommended ROE of 9.00%. Dr. Woolridge's proposed rate of return is based on his recommended cost of equity and SWEPCO's cost of debt and capital structure shown in Table 1 below:

Table 1
CARD Rate of Return Recommendation

Capital Source	Capitalization Ratios	Cost Rate	Weighted Cost Rate
Long-Term Debt	50.63%	4.18%	2.11%
Common Equity	<u>49.37%</u>	<u>9.00%</u>	<u>4.44%</u>
Total Capital	100.00%		6.56%

The record evidence fully supports Dr. Woolridge's recommended ROE. A return on equity of 9.00% is in the range of ROEs the ALJs identified as reasonable. A return on equity of 9.00% is also in the range of ROEs recommended by TIEC's expert (8.90% to 9.35%) and only five basis points below the PUCT Staff's range of ROEs (9.05% to 9.35%).¹⁴

ii. Proxy Groups

iii. DCF Model Results

iv. CAPM Model

v. Critique of Mr. D'Ascendis' ROE Recommendations

a. Capital Market Conditions

b. D'Ascendis' DCF Analysis

c. Risk Premium Approach

d. CAPM Approach

e. Use of Non-Price Regulated Companies

f. Adjustments for SWEPCO's Size and Credit-Ratings

2. Cost of Debt

B. Capital Structure [PO Issue 7]

C. Financial Integrity, Including "Ring Fencing" [PO Issue 9]

IV. Expenses [PO Issues 1, 14, 24, 29, 30, 32, 33, 40, 41, 42, 44, 45, 46, 49, 72, 73, 74]

A. Transmission and Distribution O&M Expenses [PO Issue 14, 24]

1. Transmission O&M Expense [PO Issue 24]

2. Transmission expense and revenues under FERC-approved tariff [PO Issue 46]

¹⁴ See PFD at 103.

3. **Proposed Deferral of SPP Wholesale Transmission Costs [PO Issues 72, 73, 74]**
 4. **Distribution O&M Expense [PO Issue 24]**
 5. **Distribution Veg Mgmt Expense & Program Expansion [PO Issue 27]**
 6. **Allocated Transmission Expenses related to retail behind-the-meter generation**
- B. Generation O&M Expense**
1. **Dolet Hills Non-Fuel O&M**
 - a. **Dolet Hills Net Capacity Factor Has Continued to Decline**
 2. **Retired Gas-Fired Generating Units Non-Fuel O&M Expense**
- C. Labor Related Expenses**
1. **Payroll Expenses**
 2. **Incentive Compensation**
 - a. **Short-Term Incentive Compensation**
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1. **Net Salvage/Demolition Study**
 - a. **Contingency Factors**
 - b. **Escalation Rate**
 2. **Service Lives**
- E. Purchased Capacity Expense**
1. **SWEPCO's Cajun Contract**

VII. Revenue Distribution and Rate Design [PO Issues 4, 5, 47, 48, 52, 59, 60, 61, 62, 75, 76, 77, 78, 79]

A. Rate Moderation / Gradualism [PO Issue 52]

- 1. Nucor Steel's Recommended Rate Moderation Plan**
- 2. Staff's Recommended Four-Year Phased-In Rate Moderation Plan**

B. Rate Design and Tariff Changes [PO Issues 60, 61, 62]

C. Transmission Rate for retail behind-the-meter generation

D. Riders [PO Issues 47, 48, 75, 76, 77, 78, 79]

- 1. Proposed Residential Service Plug-in Electric Vehicle Rider [PO Issues 75, 76, 77, 78, 79]**
- 2. Renewable Energy Credit Rider [PO Issues 47, 48]**

E. Retail Choice Pilot Project

VIII. Baselines for Cost-Recovery Factors [PO Issue 4, 5, 52, 63]

A. Interim Transmission Cost of Service

B. Transmission Cost Recovery Factor

C. Distribution Cost Recovery Factor

D. Generation Cost Recovery Rider

IX. Reasonableness & Recovery of Rate Case Expenses [PO Issues 26, 27, 28]

X. Other Issues [including but not limited to PO Issues]

A. Additional issues

B. CWIP [PO Issue 17]

C. Cash Working Capital [PO Issue 18]

D. Administrative and General O&M Expenses [PO Issue 25]

E. Tax savings from liberalized depreciation [PO Issue 34]

- F. Advertising expense [PO Issue 35]**
- G. Competitive affiliates [PO Issue 43]**
- H. Deferred Costs [PO Issue 50, 51]**
- I. Proposed Time-of-Use Rate Pilot Projects [PO Issues 80, 81, 82, 83, 84, 85]**
- J. Experimental Economic Development Rider**
- K. Any exceptions requested to PUC rules [PO Issue 64]**
- L. Should PUC approve requests for waivers? [PO Issue 65]**
- M. Compliance with Dkt. 46449 [PO Issue 66]**

XI. Conclusion

CARD respectfully urges the Commission to grant CARD's Exceptions to the Proposal for Decision and to make such other findings consistent with the recommendations CARD has made in both its initial and reply briefs and in these Reply to Exceptions.

Respectfully submitted,

HERRERA LAW & ASSOCIATES, PLLC

P.O. Box 302799
Austin, Texas 78703
4524 Burnet Road
Austin, Texas 78756
(512) 474-1492 (voice)
(512) 474-2507 (fax)

By: /s/ Alfred R. Herrera

Alfred R. Herrera
State Bar No. 09529600
aherrera@herreralawpllc.com

Sergio E. Herrera
State Bar No. 24109999
sherrera@herreralawpllc.com

service@herreralawpllc.com

**ATTORNEYS FOR CITIES ADVOCATING
REASONABLE DEREGULATION**

CERTIFICATE OF SERVICE

I hereby certify that on this the 28th day of October, 2021 a true and correct copy of the *Cities Advocating Reasonable Deregulation's Reply to Exceptions to the Proposal for Decision* was served upon all parties via electronic mail in compliance with SOAH Orders Nos. 4 and 13, and with the Commission's Order Suspending Rules, issued in Project No. 50664.

By: /s/ Leslie Lindsey

Leslie Lindsey